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Via E-mail

May 2, 2006

Karl Fingerhood, Esq.
Trial Attorney - Environmental Enforcement
Section
U.S. Department of Justice
Environment and Natural Resources Division
P.O. Box 7611
Washington, D.C. 20044-7611

Re: U.S. v. Powerine, et al.

Dear Karl:

On April 21, 2006, you sent me an e-mail suggesting that Powerine Oil Company, CENCO Refining Company, and Energy Merchant Corp. (collectively "Powerine") present the United States with a settlement offer. This letter is in response to that request.

At the outset, we have amply demonstrated to the United States that Powerine does not have the financial ability to make any significant payments to resolve this matter. Our consultant, LECG, has run the EPA's ABEL model on the data provided to the EPA. LECG has informed us that, even when the analysis is run assuming a \$1 contribution to clean up costs, the conclusion section of the ABEL model states, among other things:

1. ABEL estimates a less than 50% probability that Energy Merchant Corp. can currently afford a \$1 contribution (pre-tax); and
2. ABEL estimates a 70% probability that Energy Merchant Corporation could afford to pay a \$0 contribution (pre-tax).

The probability of being able to pay more would be significantly less. We have not received any comments from EPA or the Department of Justice indicating that they question Powerine's difficult financial situation.

In addition, we have demonstrated to the United States that the limited resources which are available to Powerine are all needed to address other pressing environmental problems including the investigation and cleanup of the former Powerine Refinery site (the "Refinery Site"). As the United States is aware, Powerine is subject to Cleanup and Abatement Order No. 97-118 ("CAO") issued by the California Regional Water Quality Control Board requiring it to cleanup and abate the Refinery Site. In addition, the City of Santa Fe Springs filed a suit under the City's Polanco Act pursuant to which it obtained an injunction compelling Powerine's compliance with the CAO. In addition, the City of Santa Fe Springs is putting considerable pressure upon Powerine to complete this effort as soon as possible or face legal consequences.

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Thus, we provided the United States with an estimate prepared by Powerine's consultant estimating that it will cost between \$18 million and \$27 million to address soil and groundwater contamination at the refinery site. In addition, Powerine is expected to incur approximately \$2.7 million to abandon the numerous wells located at the site.¹ As indicated in my March 13, 2006 letter to the United States, Powerine will also have to remove and dispose of the surface structures which include a large number of tanks, large amounts of piping and asbestos containing material, and subsurface structures such as foundations, piping and utility systems. Powerine estimates that it will cost an additional \$5 million to \$10 million to complete this effort. Thus, Powerine estimates that the cost to address the refinery site alone is in the range of \$26 million to \$40 million. This figure, however, does not include the staff and other carrying costs for the refinery site which Powerine estimates to be in the range of \$300,000 per month. Assuming that it will take approximately four years to complete the investigation and cleanup,² the carrying costs add an additional \$14.4 million to this figure. Thus, the total cleanup costs for the refinery site, including carrying charges, are estimated to be in the range of \$40 million to \$54 million.

In addition, Powerine faces other significant environmental liabilities. For example, Powerine leased a parcel of land at the southeast corner of Lakeland to store jet fuel in two aboveground storage tanks. Powerine estimates that the cost to investigate this location will be in the range of \$750,000 to \$1 million, primarily because recent groundwater monitoring shows the presence of significant free product in the groundwater. The cleanup costs is still uncertain. Both the City and the RWQCB contend that Powerine is the source of this contamination. Powerine also owns a pipeline which extends from a terminal in Huntington Beach, out one and a half miles. The pipeline is subject to a lease with the State Lands Commission which requires that the pipeline be removed. While Powerine is exploring options for the continued use of the pipeline, the costs to remove it are estimated to be in the range of \$5 million. In addition, Powerine owns over 60 miles of pipelines throughout the Los Angeles area. Powerine estimates that the potential liability associated with the pipelines is in the range of \$10 million to \$20 million. Powerine also faces environmental risks associated with numerous gasoline station sites which it operated over the years. Thus, Powerine's non-refinery site liabilities are estimated to be in the range of \$20 to \$25 million.³

In sum, Powerine's potential environmental liabilities, aside from those associated with the WDI Site, are in the range of \$55 million to \$75 million. As noted above, the ABEL model confirms

¹ This was the figure used in our last submission. This was at the low end of the range. The cost to remove the wells could be as much as \$4 to \$5 million.

² This figure is in the mid-range of BBL estimate that it will take between two to six years to complete the cleanup.

³ Powerine is also involved in litigation with Golden West Refining and Thrifty Oil Company ("Thrifty") which are seeking in excess of \$600,000 in damages from Powerine relating to the Huntington Beach terminal facility formerly operated by Thrifty.



that Powerine does not have an income stream which is likely to generate any significant cash which can be used to address these liabilities.⁴

Nevertheless, in order to put this matter behind it so that it can concentrate on the refinery cleanup and put its limited financial resources into that effort rather than into litigation, Powerine is willing to make an offer to resolve this matter. In the past, Powerine suggested that EPA accept proceeds from an insurance policy issued by Harbor Insurance. Powerine, however, understands the government's reluctance to accept such an arrangement, particularly given the uncertainties associated with the policy and its \$50,000 limit. Therefore, Powerine understands EPA's desire for cash rather than a contingent payment based upon an uncertain insurance recovery.

In order to come up with an appropriate settlement figure, we reviewed the history of settlement negotiations between the United States and Powerine. During the mid to late 1990's, EPA and Powerine entered into settlement discussions regarding this matter. Powerine asserted then, as it does today, that it was in dire financial straits and, therefore, could not make a substantial payment. EPA agreed and, in early 1996, EPA and Powerine reached a tentative agreement to resolve this matter for a payment of between \$200,000 and \$250,000.⁵ At the time, EPA's projected remedial costs were \$5,200,000 and its past costs totaled \$6,000,000. Thus, the total site costs were projected to be approximately \$11.2 million. Thus, EPA and Powerine agreed to settle for a figure which represented approximately 2% of the site cleanup costs. Powerine believes that this 2% figure should serve as a basis for a settlement of this matter.

EPA currently estimates the total past and future response costs for the WDI Site will be in the range of \$30 million. Therefore, Powerine is willing to settle this matter for a cash payment of

⁴ Powerine will also attempt to require its insurance carriers to fund some portion of the required environmental work. However, given the exclusions in the policies, most of those that remain have either "sudden and accidental" or so-called "absolute" pollution exclusions, it is difficult to predict how much the carriers will contribute to the actual cleanup.

⁵ Our records indicate that EPA initially offered to settle for \$500,000, Powerine countered with an offer of \$200,000 and EPA then verbally indicated a willingness to settle for \$250,000. However, for reasons which are now unclear, these settlement negotiations were never finalized. It was not until a few years later, in early 1999, that EPA raised concerns about the sale of Powerine's assets to CENCO and the transfer of some of the proceeds to EMC. As demonstrated in detail in Powerine's July 15, 2005 letter to the United States, that transfer did not constitute a fraudulent conveyance because Powerine was not rendered insolvent. CENCO assumed the liabilities and agreed to fully indemnify Powerine and insurance was anticipated to be available to cover some of the environmental liabilities. In any event, Powerine has demonstrated that all of those funds were retained by EMC, used as part of its routine operations, and are no longer available.



2% of this figure or \$600,000. This is more than twice what EPA agreed to accept in 1996 and more than EPA initially offered in 1995.⁶

We would like to meet with you at your earliest convenience to discuss this offer and to attempt to reach a quick resolution which will allow us to concentrate our efforts on refinery site cleanup rather than litigation.

Please feel free to call if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Albert M. Cohen".

Albert M. Cohen
of Loeb & Loeb LLP

AMC:amc
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cc: Vincent Papa

⁶ This figure is contingent upon a full release and covenant not to sue consistent with the requirements of CERCLA as well as contribution protection. The releases would have to cover the Operating Industries, Inc. site as well as the WDI Site. The releases would also have to cover all related individuals and entities including the Rothschilds.